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SUBJECT: WIDENING BALANCE OF PAYMENTS DEFICIT SPARKS CONCERN

REF: A. 08 RABAT 893
¶B. 08 RABAT 853
¶C. 08 RABAT 254
¶D. 09 RABAT 190
¶E. 09 RABAT 276

¶1. (U) Summary: Last year's sudden swing into the red of Morocco's balance of payments has sparked increasing concern that the country's international position remains its key vulnerability in confronting the world economic downturn. After years of surplus and a narrow deficit (0.1 percent of GDP) in 2007, the current account deficit grew to 4.8 percent of GDP in 2008, as declining remittances, investment flows, and tourism revenues could not counterbalance the country's structural commercial deficit. Analysts are divided on what the future holds, with some holding out hope that declining commodity prices will improve the situation, but Morocco's weakening international position has led to intensification of efforts to remedy the woes that beset the country's export sector (Ref B). End Summary.

CURRENT ACCOUNT IN THE RED

¶2. (U) In their recent public comments, Moroccan public officials have underlined the strong position from which Morocco confronts the international financial crisis. They concede, however, that the one chink in its armor is its burgeoning balance of payments deficit, which reached 4.8 percent in 2008. The country has enjoyed a surplus or near balance since 2001, but in fact the positive figures concealed increasing weakness in the country's trade balance, as imports repeatedly outstripped exports and ultimately left the country with an export/import coverage ratio of less than 50 percent. "It was easy to overlook the problem," National Export Council Noureddine Omary told us in a recent meeting, "when tourism income, remittances, and investment took up the slack." Now, however, those elements are also under pressure as a result of the international conjuncture, and Morocco faces the prospect of balance of payments deficits into the future, unless its export offer can be made more competitive.

¶3. (SBU) The recent release by the Moroccan Treasury of balance of payments statistics for 2008 highlights the increasing imbalance in Morocco's economic interaction with the world, an issue that has prompted much discussion and soul searching regarding the country's efforts to liberalize its trading relations with the EU, U.S., and others (Ref E reports on a recent analysis of the impact of the free trade push, commissioned by Morocco's influential General Confederation of Moroccan Enterprises (CGEM)). While Moroccan exports and imports grew by a similar percentage in 2008 (24.3 percent and 23.9 percent respectively), imports did so from a much larger base, rising by USD 8 billion, more than double the USD 3.9 billion increase in exports. More

worrisome for Morocco, virtually the entire increase in exports came from phosphates and phosphate derivatives. Other exports were essentially flat, increasing only 1.2 percent.

OTHER SECTORS NO LONGER TAKE UP THE SLACK

¶4. (SBU) Morocco has long had a structural trade deficit, so the shortfall is not surprising. What sparks concern now is not just that imports continue to outpace exports by a significant margin, but that the flows that have historically counterbalanced it are all under threat from the international economic downturn. In recent years, the trade deficit has been covered by remittances and services (primarily tourism) income. Both have waned as the crisis has hit home in Europe, the source of 90 percent of Morocco's tourists and the home of 90 percent of its expatriates. Tourism receipts fell 3.5 percent to USD 7.3 billion in 2008, while remittances from Moroccans abroad fell 2.4 percent to USD 6.9 billion. The overall balance of payments deficit thus increased to 4.8 percent of GDP. Foreign investment also tumbled by 23.3 percent to USD 4.1 billion, still above the average for the last five years, but not sufficient to permit Morocco to maintain its foreign reserves, which slipped by USD 826 million to USD 23.4 billion, the equivalent of only 6.2 months of imports. In his public presentation of Morocco's economic situation in mid-March, as in a meeting with us earlier this month, Treasury Director Chorfi noted that while overall he alternates between "quiet confidence" and "preoccupation" about Morocco's situation, it is Morocco's international position that he believes constitutes the country's principal vulnerability.

¶5. (SBU) A number of our contacts are quick to nuance this concern, however. As a contact in the financial community reminded us last fall, unlike those countries in Eastern Europe and elsewhere that were reliant on international financing, Morocco has largely financed itself. Foreign direct investment expanded dramatically in recent years, but in a sense was the icing on the cake, and was not critical to financing either the central government or the country's balance of payments. Others argue too that the way in which terms of trade are evolving as a result of the crisis will work in Morocco's favor. Karim El Aynaoui, the Bank Al-Maghrib's Director of Studies, downplayed concern about the balance of payments at a conference last month, pointing out that more than a third of the increase in imports in 2008 stemmed from soaring global energy and food prices. He conceded that both imports and exports will decline as a result of the crisis, but argued that the "base effect" will work in Morocco's favor, precisely because imports are so large. If both exports and imports decline 10 percent as a result of the crisis, as he anticipates, the country's trade deficit will decline by a similar percentage.

EXPORT WEAKNESSES

¶6. (SBU) Skeptics, however, point to the fact that Moroccan exports may be even more vulnerable than imports to the changing terms of trade. They note that phosphate exports grew in value last year by 130 percent or USD 3.7 billion, on the base of a declining absolute volume. Given that phosphate prices have fallen sharply this year, they warn that the decline in exports may actually outstrip that of imports, and not improve the trade balance. Others note too that the headline export figure for Morocco is misleading, in that much of the total consists of goods that were imported for final processing. The portion of Moroccan exports that actually reflects value added in Morocco, Nezha Lahrichi, head of the Moroccan Export Insurance Company (SMAEX) recently suggested, is only 30 percent of the official USD 19.9 billion figure.

¶7. (SBU) Recently released statistics from the Office of

Exchanges for the first two months of 2009 are mixed, but hint that the more pessimistic vision may ultimately be closer to the mark. The export decline outpaced the decline in imports (31.8 to 15.6 percent). The base effect left the trade deficit virtually unchanged from last year, but the import/export coverage ratio slipped dramatically from 49.7 to 40.2 percent. For the two months, tourist receipts and remittances continued their slide, declining 14.2 and 16.1 percent respectively. Investment income was off 48.3 percent in January, but made up that shortfall in February, totaling USD 840 million for the two months, up 16.1 percent over ¶2008. (Note: Notwithstanding this positive news, a number of high profile projects are under threat, and the GOM base case scenario assumes a significant drop in investment for the year. End note.)

¶8. (SBU) The mixed picture has focused attention in the Government of Morocco not just on the conjunctural effects of the current international slowdown, but on the overall failure of the government's export strategy. Morocco's new "Maroc Export" strategy addresses the trade promotion side of the equation, but as observers from Noureddine Omary of the CNCE to Roving Ambassador and former Trade Minister Hassan Abouyoub point out, the larger problem is Morocco's failure to accompany the free trade push with strategies to develop either promising export-oriented sectors or "national champions" that could lead the outward push. Abouyoub argues that free trade agreements "cannot provide miraculous remedies to underlying dysfunctionalities in the economy," and that the benefit Morocco gained from its earlier structural reforms before 1995 is now largely eroded. As a result, the economy is largely dependent on internal demand and investment, with the external sector dragging down GDP rather than contributing to it.

¶9. (SBU) Comment: If the diagnosis is clear, appropriate remedies remain elusive. Refs B and D reported on the Moroccan government's initial steps to address shortcomings in its export promotion efforts, but experts concede that while this is a part of the solution, it is far from the most important one. Marrying promotion to appropriate sectoral reforms and incentives is even more critical. The Government of Morocco is only now tackling this challenge with the second phase of the Emergence Program, an initiative for industrial development aimed at supporting and increasing the global competitiveness of key export sectors, including automobile and aeronautics, offshoring, and textiles. End Comment.

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